The functional role of behavioral trust in mudarabah financing agreement: A conceptual framework

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Abstract

Trust represents the foundation of mudarabah contract, but its functional role in such contract is far from clear. In the Islamic literature trust-based decision has been constructed as it has two aspects. The first represents the cognitive aspect, and the second represents the dogmatic aspect. The cognitive aspect of the trust is formed while exerting the due efforts in order to reinforce a satisfactory level of cognitive confidence. The dogmatic aspect is represented by the optimistic hope of achieving the desirable consequences of the trust-based decision. Trust-based decision itself is about acceptance of the exposure to a potential occurrence of undesired outcome of engaging in agreements with others. We explain how both the cognitive and the affective aspects of trust participate together in shaping its behavioral aspect when the bank becomes the capital provider on mudarabah basis. First, we argue that exerting the due efforts is the cause of mitigating the uncertainty inherent in the mudarabah agreement and producing a state of cognitive confidence sufficient to put the bank management in a trusting situation. Second, we show how affective trust is needed to enable the trust-based decision concerning the mudarabah financing agreement. Third, we argue that accepting the exposure to a potential occurrence of undesired outcome of engaging in this agreement represents the behavioral manifestation of trust.

Keywords: *behavoiral trust, trustworthiness, uncertainty, islamic norms, mudarabah financing agreement.*

1. Introduction

Trust is a critical constituent of all human relationships, and has traditionally received considerable attention in the literature across many disciplines. In the Arabic lexicon the term trust '*thiqah'* has several meanings which range among three constructs

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namely: belief, behavior or decision.The term '*thiqah'* means entrusting the others '*I'timan'*, delegation '*Tafweedh'*, reliance '*Tawakkul'*, dependence '*I'timad'* and any other meanings which assign a state of acceptance of being contingent upon uncertain factors. Trust per Webster's Ninth Collegiate Dictionary has several definitions. For example, it is defined as *"confidence in and reliance on good qualities, especially fairness, truth, honor, or ability"*, it is also defined as *"an assured reliance on the character, ability, strength, or truth of someone or something one in which confidence is placed",* or as *"dependence on something future or contingent", and as "a hopeful reliance on what will happen in the future"*.

In Islam, the concept of trust is considered as a very influential and fundamental inspiration in all aspects of Muslims' lives. Allah, the Most Exalted, wants trust to be prevalent among people at the individual and social levels as well as at the level of the entire nation and reality. Allah defined successful believers as ones who uphold their trusts and covenants.

Allah says in His Glorious Book: "Successful indeed are the believers" ……. "Those who are faithfully true to their amanat (all the duties which allah has ordained, honesty, moral responsibility and trusts) and to their covenants" (Al-Mu'minun: 1,8). Allah wants the people, to observe their trusts and do not betray it. He says in His Glorious Book: "Then if one of you entrust the other, let the one who is entrusted discharge his trust (faithfully), and let him be afraid of Allah" (Al-Baqarah: 283) And in another versus Allah says: "Verily! Allah commands you that you should render back the trusts to those whom they are due" (An-Nisa: 58)

In Islamic banking context the trust *thiqah* concept represents the foundation element of a variety of Islamic financing products such as mudarabah, musharakah, bai al salam, bai bithaman ajil (BBA), istisna'a and any other financing products whose specify a moral obligation on one or both of the transacting parties and have underpinning level of uncertainty concerning the ability and willingness to fulfill that obligation.

For example, mudarabah agreement is based on a fiduciary relationship (aqd alamanah) where the entrepreneur (mudarib) manages the mudarabah asset in trust i.e. has a moral obligation to perform in full integrity, and in the best manner, to achieve the desired aim of the capital provider, who has no control on the management and the operation of the business. Additionally, in mudarabah financing agreement, uncertainty concerning the mudarib's abilities, performance and incentives are extremely high because of the information asymmetry which may lead to both adverse selection and

moral hazard problems (Boubah, 2009). Mudarabah financing agreement is, in general, uncollateralized and therefore capital provider usually has to rely on faith, trust, and a sound confidence in the entrepreneur (Kayed, 2012), and his expectations about the entrepreneur's quality (skills and expertise) and trustworthiness are of paramount importance.

Trust also represents the foundation element of bai al salam agreement. In such mode of financing, the sale of an object is made even though such object is not available at the time of the conclusion of the sale, but rather it is agreed to be delivered on a future fixed date. The price is, however, must be paid immediately during the session of the agreement. Such sale agreement will also create a moral obligation where the seller undertakes to supply the determinate object on the future pre-agreed date.

Similarly, the element of trust could also be traced in the istisna'a financing agreement. Istisna'a is a request to manufacture particular objects by others (manufacturers). Practically, it is an agreement to purchase, for a definite price to be paid in advance or on completion, an object that may be manufactured later in accordance to pre-agreed specifications between the parties. Thus, the istisna'a agreement creates a moral obligation on the manufacturer part to manufacture the object, and who is expected to possess the required skills, expertise or craftsmanship to manufacture the underlying object as exactly specified.

Given the complex conceptualizations of trust, we firstly review the literature on trust and its related concepts. Secondly, we propose a framework of three distinct, but related aspects of trust — cognitive trust, affective trust and behavioral trust. We then develop and analyze the relationships among these three aspects. Our purpose here is to investigate the Islamic-based view of trust, and to attempt to explain how this concept functions when involving in mudarabah agreement.

2. Behavioral/Intentional Aspect of Trust

Many scholars have acknowledged trust to be treated as behavior e.g.(D Harrison McKnight, 2001; Lewis & Weigert, 1985; Mayer, Davis, & Schoorman, 1995) Behavioral trust is the actual assuming of risk or becoming vulnerable (Mayer et al., 1995). (McKnight & Chervany, 2000) defined trust as a behavior of the trustor's being willingly and tranquilly dependent on the trustee's discretion to act even in a situation in which negative contingencies are potential. Trust-related behavior is manifested

where a trustor gives a trustee a "fiduciary obligation" (Barber, 1983)i.e. where the trustor make himself as being betrayed by the trustee. According to (McKnight & Chervany, 2000), the behavioral aspect is specified by using the term 'dependence' to differentiate between the trust-related behavior and the trusting intention. He mentioned that some trust-related behavior could be represented in behaviors such as decreasing control, accepting influence, granting anatomy and transacting business. For example, Reducing the rules and the controls that the trustor imposes to restrict the trusree's actions (Baier, 1986) will expose the trustor to higher level of risk because he has to be more dependent on the trustee's discretion since the trustor does not have the ability to direct the trustee's actions (McKnight & Chervany, 2000). To be considered as a trust related behavior it should implies the trustor's acceptance of the exposure to uncertain factors.

A number of scholars have also conceptualized trust as a behavioral intention e.g. (Mayer et al., 1995; McKnight & Chervany, 2000; McKnight, Cummings, & Chervany, 1998; Rousseau, Sitkin, Burt, & Camerer, 1998). According to (McKnight & Chervany, 2000), trusting intention is the trustor's solid willingness to be tranquilly dependent on the trustee's discretion to act even in a situation of lacking control over that trusree or even in a situation in which negative contingencies are potential. (Mayer et al., 1995) defined the intention or the willingness to be dependent as the trustor's readiness to make himself vulnerable to the action of the trustee by tranquilly relying on him. The readiness or the willingness of the trustor to be dependent is of a central importance in clarifying the difference between the trusting behavior and the trusting intention (Lewis & Weigert, 1985; Mayer et al., 1995). To be tranquilly dependent means that when the trustor depends on the trustee's discretion to act he does not have anxiety of fear but, instead, he is comfortable, and confident (Lewis & Weigert, 1985). Behavioural intentional models are conceptually addressed by the theory of reasoned action (Fishbein & Ajzen, 1975) and the theory of planned behaviour (Ajzen, 1991). These models generally state that attitude toward the behaviour, subjective norm, and perceived control predict intention and that intention predicts behaviour.

3. Cognitive Aspect of Trust

The literature views trust as it can develop through cognitions, calculations, or rational. According to rational choice theory, individuals are presumably motivated to make rational choices by maximizing the expected gains or minimize the expected losses

from their transactions. (Schelling, 1980) stated that choices are motivated by a conscious calculation of advantages. The rational choice perspective finds its roots in economic theories such as transaction cost theory (Williamson, 1993), and strongly affects the conventional conception of trust within the organizational theory. (Johnson & Grayson, 2005) argue that cognitive-based trust emerges because of the accumulated knowledge that enables the trustor, with certain level of confidence, to make rational decisions in assessing the trustee's trustworthiness. (Lewis & Weigert, 1985) defined cognitive-based trust as a cognitive assessment that differentiates among persons and institutions based on how the trustor perceives their trustworthiness. They argued that the choice of the trustor to behaviorally trust others could be based on "good rational reasons", and these reasons act as a proof concerning the trustee's trustworthiness and to support the acceptability of decision alternatives (Pennington & Hastie, 1993) .Reasons theory (Westaby & Fishbein, 1996) suggests that reasons motivate behaviour, because they help people justify and defend their actions (Westaby, 2005) . (Pennington & Hastie, 1993) also argued that the decision maker will likely choose an alternative with confidence as long as the explanation for this alternative is strongly backed with supporting reasons.

However, in spite of acknowledging the importance of the cognitive aspect to understand the concept of trust, some concerns regarding such aspect have been invoked by several researchers (Lewis & Weigert, 1985; Mayer et al., 1995; McAllister, 1995). These researchers argued that there is a need to a more complex and multidimensional conception of trust which includes psychological and affective components. Addressing the cognitive aspect of trust alone does not provide a comprehensive understanding of the concept of trust as noted by (Fine & Holyfield, 1996). (Kramer, 1999) contented that basing the decision to trust only on the conscious calculations and in compliance with the assumptions of rational choice models is insufficient, this is because many of the presumptions of such models, he argues, are empirically lacking the sound reasoning, and assign only a negligible role to the affective and the social impacts on trust-based decisions. (Granovetter, 1985) argued that rational-choice-based conception of trust offers, at best, an under-socialized conception of trust. (Olsen & March, 1989)have gone further by excluding the idea that rational choice and calculation to be even pivotal for addressing the concept of trust.

4. Affective Relational and Dogmatic Aspects of Trust

As a reaction to the above mentioned concerns, it has been suggested by several scholars (Kramer & Tyler, 1995; McAllister, 1995) that social, cultural and relational foundations of trust-related decisions must sufficiently and methodically incorporated in the theory of organizational trust. These scholars opined that beside the rational, cognitive and calculative orientations toward risk social, affective and relational orientations toward other people and toward society as a whole is also needed. For example, (Fine & Holyfield, 1996) suggested that beside the cognitive aspect of trust, the conceptualization of trust must also incorporate aspects such as cultural implications, affective reactions and social underpinnings. Conventionally, an empirical attention has been paid to the affective-based trust among management and marketing researchers. Their studies have found several antecedents and consequences of affective-based trust. (Johnson & Grayson, 2005) for example, found that the frequency of the former interactions between the trustor and the trustee as well as altruistic behavior, are affective foundation of trust. They also found that affective-based trust has a positive influence on the trustor's anticipation of future interaction with the trustee. In (Schoorman, Mayer, & Davis, 2007)they argued that although the perceptions of others and perceptions of risk inherent in the behaviors being considered must be considered in order to come to decisions about taking risks, emotions do influence the perception of the antecedents of trust. They think the role of emotions is a very interesting area of research and will add a new dimension to the model.

Beside the affective and the relational aspect, trust also has dogmatic aspect. The most basic illustration of the dogmatic aspect of trust is represented in its relation to doctrines morals, norms and faith. (Simmel, 1950) recognized a "further element", described as a sort of faith-based element which is essential to explain the unique nature of trust. He stated that the conception of trust includes a further element of quasi-religious faith within trust, this element concerns a state of mind which has nothing to do with knowledge.

From Islamic perspective, one construct that is inherently woven into the conceptualization of trust is reliance (Al-Twakkul). Tawakkul eases the likelihood of the bank's acceptance to involve with a particular entrepreneur in a business relationship even where the information about that entrepreneur, and about the future contingencies that might affect the future outcome of such relationship, is asymmetric. Reliance on Allah (the All Mighty), in this sense, represents the faith-based or the dogmatic aspect which always should go hand in hand with the cognitive aspect when addressing the

conception of behavioural trust. Conceptually, Muslims rely on their lord in all affairs, which indispensably necessitates the presence of reliance element in every behaviour, action and decision a Muslim makes and, at the same time, differentiates the Islamic conception from the conventional conception of the trust.

The meaning of reliance can be deemed from the following: In Quran, Allah directs His believers to rely on Him (e.g. 3:159, 160; 5: 23; 39: 38; 65: 3). Anas bin malik said: (a man said to the messenger of Allah: should I hobble it (his camel) and rely (on Allah), or bridle it and rely? He (the messenger of Allah) said: bridle it and rely).

Reliance on Allah is interfused with the faith element, In Quraan several versus indicate to this relationship between faith and reliance. For example, Allah (The Most High) says: "The believers are only those who, when Allah is mentioned, feel a fear in their hearts and when His Verses are recited to them, they increase their faith; and they rely on their Lord" (8:2).In another versus Allah (the most High) says: "Say: He is the Most Gracious (Allah) in Him we believe, and on Him we rely. So, you will come to know who it is that is in manifest error" (67:29)

Ibnu Al Qayyem In *Madaarij us-Saalikeen* explained reliance concept as follow: reliance on Allah is an affective state i.e. a state of the heart, which emerges because of knowing Allah All Mighty and realizing that only He who creates, arranges, harms, benefits, gives, deprives, and because of knowing that whatever Allah all mighty wants to happen will happen even though people don't want it to happen, and whatever he doesn't want to happen will not happen even though people want it to happen. Thus, as a result, the slave should depend on his lord, and delegate his affairs to him with tranquility and certitude that Allah will sufficiently arranges the delegated affairs for him (Ibnu Al Qayyem Al Jawziah v. 82). Imam Al Ghazali defined the reliance on allah as a belief in the unseen after doing one's best or utmost diligence determined in the worldly seen life; a belief in God after performing all self-related duties (Al Ghazali ب: ت: 277).

Exerting the due effort *Al Akhzu bil Asbab* is another fundamental Islamic norm that is related to dogmatic aspect of trust. Muslims embrace and practice this norm in all aspect of their daily life if they are willing to achieve the desirable consequences (al falah) of their deeds in the daily life and in the hereafter. There is many of the glorious Qur'anic verses teaching Muslims that related due efforts should be made if they want to achieve the consequences they desire (e.g. 1:282; 4:102; 8:60; 16:32; 16:97; 18:83; 19:25). In

verse (1:282) for example, Allah, All Mighty, oriented the believers to write down the debt to use this writing as a proof when the debtor deny the debt or procrastinate to pay it back if they want to protect their wealth. In the banking context, banks are required, while practicing their intermediary role, to acquire and utilize the available information about the entrepreneur's personal and professional traits, or about the feasibility of the mudarabah enterprise. Exerting such efforts reduces the information asymmetry, mitigates the uncertainty that is inherent in mudarabah financing agreement, and reinforces the rationality of the trust-based financing decisions made banks.

In the Islamic normative scheme the two fundamental concepts namely: exerting the due effort and reliance have different meanings but always attached and complete the meaning of each other. This meaning is clearly stated in the following: In Al-Quran (3:159) God All Almighty said:

> '*And when you are resolved on a course of action, place your trust in Allah; surely Allah loves those who put their trust* (in Him)'.

In the meaning of this verses sheikh Al Tantawi in Al Tafsir Al Wasit stated that: if you intended to carry out an action after enough consultation with the thoughtful involved expertise and after the appositeness of this intended action becomes clear, take the initiative by carrying it out without hesitation that might change the advantages of the action into disadvantages, and trust in Allah and depend on Him, and believe that He is Allah All Mighty Who created the causes and created what makes this causes.

In the above mentioned Hadith our prophet (peace be upon him) clarify that to rely on Allah in keeping the man's animal of going astray is not enough unless the man take a necessary action and bridle it.

Ibnu Al Qayyem stated that: trust in Allah and reliance on him should be accompanied with exerting the due effort, otherwise, a violation of shariah commands and its wisdom occurs. Thus, the two above mentioned statements stipulate that the meaning of the reliance will not be sound unless all the related necessary and possible efforts are exerted.

The dogmatic-based trust completes the meaningfulness of cognitive-based trust. (McAllister, 1995) argued that some level of cognitive-based trust is necessary for affective-based trust to develop. The idea underlying that approach is that the trustor will not engage in relationship before obtaining some evidence of the trustee's

trustworthiness. According to (McAllister, 1995), the required evidence will be obtained through cognition and, for that reason, cognitions precede affects.

5. Trust-Based Decision Uncertainty Risk and Knowledge

Normally, the economic activities and transactions which have added-value in order to generate returns involve a particular level of inherent uncertainty. Keynes, in his General Theory showed that, in the absence of complete certainty about the future, one can make rational decisions by looking not only at the probability estimates but also at the weight of argument that support this probability. He defined the weight of argument as the as the level of completeness of the information set on which a probability assessment is based.

(Crocco, 2002) have argued that the in Keynesian sense is plausible to develop a concept of degree of uncertainty. These authors have based their argument on Keynse's definition of weight of argument. For example, (Crocco, 2002) argued that the concept of weight of argument could be used to understand uncertainty as a concept feasible to be leveled. In other words, the degree of completeness of the information could be viewed as the measurement of the degree of uncertainty. For example, a complete absence of knowledge could be explained as an extreme case of uncertainty in a trusting situation. Therefore, as the weight of argument is increases uncertainty decreases. However, such uncertainty cannot be totally eliminated and can only be mitigated by financial institutions in order to be able to effectively utilize the Islamic trust-based financing such as mudarabah financing agreement. The literature emphasizes that trust exists or needed only where there is uncertainty condition about the future (Lewis & Weigert, 1985; Rousseau et al., 1998).

Uncertainty appears explicitly as a fundamental element of Keynes's theory. In monetary economy, for example, he views that fluctuations in effective demand and employment occur because in a world in which the future is uncertain or unknown, individuals prefer to retain money, postponing consumption and investment decisions. In his 1937 article entitled The General Theory of Employment, Keynes defined uncertainty as: Uncertainty is that *"We simply do not know"* (Keynes, 1937). Knight (1921) argued that uncertainty arises out of our partial knowledge which is *"neither entire ignorance nor complete and perfect information, but partial knowledge"* (1921, p. 1991). Ellsberg (1961) introduced the notion of ambiguity to refer to situations in which, due to lack of information, there is uncertainty about probabilities on events.

Given the relationship between trust and uncertainty, Trust seems particularly relevant to the mudarabah financing context, because it seems obviously that the absence of trust among the transacting parties extremely hinders or even halts their transactions. For example, several studies have point out that the usage of PLS contracts is seriously marginalized in Islamic financial institutions (IFIs) that avoid or abandon these types of contracts due to the uncertainty associated with their execution (A. W. Dusuki & Abdullah, 2006; Iqbal & Molyneux, 2005; Kuran, 2004).

By utilizing the weight concept mentioned earlier, and in order to make a rational judgment concerning the trustee's trustworthiness, banks need to acquire a certain level of knowledge that enables them to involve in a trust-based agreement such as mudarabah financing agreement. Banks as capital providers will benefit from knowing the real possessed characteristics of entrepreneurs and the quality of their proposed business enterprise. The riskiness of misplaced trust can be mitigated, but not entirely eliminated, by enhancing the amount and quality of information acquired by actors about one another.

Knowledge is directly related to certainty therefore, the financing process necessitates acquiring sufficient knowledge about the mudarib's abilities and incentives to behave in accordance with the finance agreement's terms, or about the enterprise's qualities (Saparito & Gopalakrishnan, 2009)

(Uzzi & Lancaster, 2003) categorize information used by banks when making financing decisions in to two types as hard (public) and soft (private) information. According to them, hard information is reported through standard documents such as company reports, audited financial statements, regulatory filings, advertised bid-ask spreads, price quotes, contractual stipulations, warranties, credit scoring records and other forms of prepared information accessible in the public domain. Thus, hard information is verifiable across exchange partners.

In contrast to hard information, soft information is not publicly available. Rather, it is private information that references personal and nonstandard information about the finance seeker such as distinctive competencies, underlying motives, and unpublished aspects of the firm's strategy. These data are valuable to the learning process because their uniqueness furnishes prospects for innovations or cost savings that could not be provided by public information sources. However, because private information is not verified and is personal across exchange partners, it lacks objective benchmarks (Uzzi & Lancaster, 2003)

Due to this information asymmetry problem, businesses which have sought finance but about which hared information is not available will be deprived from acquiring the needed funds. For example, SMEs rarely have credit scoring records, or do not have reliable certified financial statements (Uzzi & Lancaster, 2003). This means that information about these firms' situation is, generally, not publicly available (Uzzi & Lancaster, 2003). This situation often results in negative outcomes for both banks and firms. For banks it creates a high level of uncertainty in making lending decisions (Uzzi & Lancaster, 2003).For firms, the uncertainty surrounding financing decisions results in constrained access to finance (Berlin & Mester, 1998).

The issue of lacking soft information could be addressed as information asymmetries matter. Banks are assumed to be uncertain about the riskiness of the business than the business itself both before and after the finance is provided. In business discipline, Islam recognizes that risk is common, but it also acknowledges that it can be managed and minimized if strategic steps are taken. Islam condemns two extremes of behavior with regard to risk. The first is total risk avoidance by obtaining profits without assuming any risk, which is the case with riba'. The second is excessive risk-taking in activities that have elements of gambling. In Islamic banking, risk is an integral part of financial transactions. According to (Dusuki, 2011), the general meaning of risk is the assessment of the uncertainty related to the future contingencies. He noted that risk generally means a measurement of unpredictability or uncertainty of future events. Unlike the conventional perspective of risk, Islam prohibited the total avoidance of risk by earning reword through usury-based transactions, or taking excessive risk through gambling. Instead, Islamic doctrines determine a justice framework of risk taking. In Islamic financial activities, the pre-condition is that investors bear the risks. This is based on the principle of "*al-ghunmu bi al-ghurmi*" which means that entitlement to profit is accompanied by responsibility for attendant expenses and possible loss.

The literature distinguishes between risk and uncertainty as different concepts. Risk is the probability of happening of an undesired outcome whose occurrence is uncertain. (Hansson, 2004) defines risk as a possible but not certain future occurrence of undesired outcome, or the probability of such an occurrence. Thus, risk is merely a statistical assessment of the probability of an undesired outcome to occur. Risk is a situation in which a decision must be made concerning a certain event where the probability distribution of which is known. Uncertainty, on the other hand, characterizes a situation

in which the probability distribution of the event does not exist or exists but it is not trusted. Keynes explains this sense in his 1937 article when he wrote:

"Our desire to hold money as a store of wealth is a barometer of the degree of our distrust of our calculations… concerning the future" (Ibid. 116).

Similarly, in order to differentiate between risk and uncertainty concepts, Knight (1921) introduced his notion of "immeasurable uncertainty". He started from the analysis of decisions to be taken in a context that, although confused by information asymmetries, can be represented through an exhaustive list of the possible states of the world. He argued that in a situation of risk, where the probability is based on frequencies of empirical observations, and the events occurrences are homogeneous but their probabilities are not known in advance, decision maker is always able to assign useful probabilities of future events on the basis of the unknown distribution of outcomes in a group of trials. However, in a situation of uncertainty, such probabilities cannot be assigned in any meaningful way.

(Knight, 1942) argued that when there is no valid basis of any kind for classifying the occurrences of the future events, and when homogeneity of these occurrences cannot be achieved, decision-makers most resort to expectations, and this is tantamount to the situation of uncertainty or trusting situation. Thus, the main distinction between risk and uncertainty, according to Knight, lies in the possibilities of classifying and homogenizing the occurrences of future events. Therefore, he contends that while risk probabilities can be insured uncertain expectations cannot.

(Shackle, 1959) rejected the use of probability measures to analyze decisions under uncertainty. He viewed that such a usage is inappropriate simply because the conditions required for its application do not exist in many relevant economic contexts. He argued that in actual situations, decision makers under uncertainty do not have a complete knowledge of the structure of the world. Thus, their choices are made among subjective representations of alternative future consequences of actions, and not from an exhaustive list of alternative future consequences.

In the same vein, (Davidson, 2011) argued that decision making process involves an environment of an immeasurable uncertainty, and in such situation the laws of probability do not apply. In sum, risk, under a probabilistic hypothesis, can be reduced to certainty i.e can be eliminated, while uncertainty cannot, in any meaningful manner, be reduced to certainty. (Guseva & Rona-Tas, 2001) argued that unless uncertainty is

transformed into rational calculation, revolving credit cannot develop on a mass scale. In other words, whenever uncertainty cannot be reduced to calculated risk, economic actors must rely on trust to sustain cooperative and economic transactions.

The passages above provide us with an insight that trust is viewed as a decision made under uncertainty. Uncertainty concept is prominent in the literature on decision making (Humphreys & Berkeley, 1985). Uncertainty constitutes a major obstacle to effective decision-making (Brunsson, 1985; McCaskey, 1988; Orasanu & Connolly, 1993)

(Shackle, 1959) identified two types of decisions as: empty decisions and crucial decisions. He considers empty decisions merely as a formal solution to a formal problem where the decision maker has complete and certain knowledge about all possible choices and all potential outcomes of each alternative. On the other hand he considers crucial (entrepreneurial) decisions to be as undertaking the first actual step of choosing among a variety of contradictory and mutually exclusive alternatives, about which it is impossible to know the relevant consequences (Shackle, 1958). Some examples of crucial decisions are investment, accumulation of wealth, and finance (Crocco, 2002).

In order to clarify the process of making decisions under uncertainty, (Shackle, 1959) identified the concept of expectation. According to this concept, the decision maker is concerned with the future outcome of his decision. As the outcome is not known in advance, the decision maker has to resort to expectations to anticipate what will be the potential outcomes. Shackle distinguished between unrealistic anticipation and expectations. In Shackle's words: *"When we speak of what the decision-maker can visualize, we mean what he can anticipate, that is what he can imagine without a sense of unrealism"* (Shackle, 1959). Similarly, (Coleman James, 1990; Gambetta, 1988) (Sztompka, 1999) argue that trusting others involves making predictions about their future actions.

According to (Keynes, 1937) the expectations, upon which investors must make decisions, is inferred from a state of their confidence as a partial solution to the problems of that uncertainty. In this sense Keynes also writes: *"The state of long-term expectation, upon which our decisions are based, does not solely depend, therefore, on the most probable forecast we can make. It also depends on the confidence in which we make this forecast."* (Keynes, 1937)

(Rousseau et al., 1998) used the expectation concept when he defined trust as the intention of one party to accept vulnerability based upon positive expectations of the

intentions or behavior of another party. (Zucker, 1987) defined positive expectations as current beliefs held by Party A of how Party B will act in the future. Consequently, from an exchange perspective, trust is committing to an exchange before you know with certainty how the other person will reciprocate (Burt & Knez, 1996)

6. Trust Ability and Trustworthiness

There are two Islamic standers considered when selecting the human resources, namely: ability and trustworthiness (al amanah). Trustworthiness is the most distinguished moral by which the rights of the others are protected, and trust among people is established. Allah (The All Mighty) in several Quranic verses orders his servants to maintain their trustworthiness. He orders His servants to give back the trusts to those whom they are belong (2: 283; 4: 58), orders them not to betray Him and his messenger, nor betray knowingly the things (amanat) entrusted to them (8:27), and related between achieving falah and trustworthiness (23: 1, 8). Prophet Mohammad (peace be upon him) related between faith and trustworthiness as a condition of the veracity of the faith when he said: "the one, who does not possess trustworthiness, does not possess faith, and the one who does not keep his pledge, is not a Muslim" (Ahmad; al-Tabarani; al-Bayhaqi). The Prophet (peace be upon him) was, before attaining prophet-hood, known among the people as the Trustworthy (AL-Ameen) for his honesty and integrity; traits we ought to abide by, for Allah wants us to model ourselves after His Messenger for He says:

"Indeed in the Messenger of Allah you have a good example to follow for him who hopes for the meeting with Allah and the Last Day, and remember Allah much" (33: 21).

Betraying trusts renders the Mumin hypocrite according to the hadith narrated by Al-Bukhari and Muslim "If he talks, he tells lies, if he promises he does not keep his promise, if he makes a covenant, he betrays it, and if he enters into a quarrel, he is shameless and does not behave fairly" Allah (the All-Mighty) urges on discharging the trust faithfully. Allah said in his glorious book: "Then if one of you entrust the other, let the one who is entrusted discharge his trust (faithfully), and let him be afraid of Allah" (2: 283). Tantawi in Al Tafsir Alwasit stated that: In this versus Allah (the All Mighty) urges on discharging the trust faithfully, especially when the trustor depends on the trustworthiness quality of the trustee i.e. when the trustor entrusts the trustee without contractually stipulating the agreement or witnessing or asking for

collateral. Therefore, trustee should show the due trustworthiness by fulfilling his due obligations, on the agreed upon time without delaying or denying, for his knowledge that he is accountable and responsible toward his Lord in the hereafter. Thus the trustor only depends on the trustworthiness quality to be available in the trustee rather than expecting or conceiving him as betrayer or evil. Shaik Al Tantawi also draws the attention that the trustworthiness quality must be the common quality of all Muslims to achieve falah in the worldly life as well as in the hereafter. Similarly, Dr. Zuhaily stated that this versus refers to that trustworthiness might be considered among transacting parties, and opines that a trustor might trust a trustee and not therefore require him to come up with substantial collateral merely because the trustor positively thinks that the trustee will not deny the rights or breach the covenants. Trustworthiness plays the role of fortifying the ability and making it immune against bad deeds and directing it to be utilized in the right deeds.

The concept of trust will be meaningful only if the mudarabah agreement involves three elements namely: a bank who entrusts a mudarib to manage the mudarabah assets. This implies that trust and trustworthiness are different concepts. (Mayer et al., 1995) and (Pennanen, 2009) characterized trustworthiness as a "trustee-specific" concept that demonstrates his characteristics. Capital providers will benefit from knowing the real possessed characteristics of entrepreneurs and the quality of their proposed business enterprise. (Hackman, 1995) stated that when making a judgment that the trustee is trustworthy, this indicates that such a trustee is able and willing to act in the interest of the trustor. (Lewis & Weigert, 1985) argued that the choice to trust could be based on "good rational reason" that are considered as a proof of trustworthiness.

The second standard i.e. ability is also considered by Islamic doctrines. Islam considers the types of persons and the level of their competencies when transacting the business, because by not considering this may cause loss of wealth. Allah the (All Mighty) directs the mankind not to give their property unto the foolish (4: 5). Ability doesn't merely refer to the physical aspects, but it also refers to all type of excellence, specialization knowledge and qualification which enables mudarib to manage the mudarabah assets in the best manner. For example, Knowledge, as was the trait that nominated prophet Yusuf (peace be upon him) to be set over the store-houses of the land (12, 55), and ability and trustworthiness were the traits that motivated the good man to choose Prophet Moses (peace be upon him) to work for him and to wed him one of his daughters (28:26). According to (Dusuki, 2011) Islamic contracts have eligibility

requirements, and one's expertise is acknowledged to have influence on the profit and loss in any investment.

In sum, a competent mudarib that can be entrusted is that one who possesses the due level of trustworthiness and has the required skills and capabilities to execute a particular action and achieve aimed outcomes assigned by the trustor. Although the conventional literature on trust has yielded a plethora of different traits to address the trustworthiness concept, only three traits have been proposed by (Mayer et al., 1995) to sufficiently and comprehensively explain the trustworthiness concept as they argued. The first trait is the ability that the trustee possesses concerning a particular domain. The second trait is the trustee's integrity which refers to the willingness of the trustee to act in a truthful manner and follow a set of accepted norms. Finally, the trustee's benevolence defined as trustee's enthusiasm and acting that display care concerning the trustor's interest. (Mayer et al., 1995) elaborated that if the trustor perceives these three traits as high, then the trustee would be rendered quite trustworthy. However, they argue that trustworthiness should be thought of as a continuum rather than the trustee being either trustworthy or not.

7. Trust and Social Capital

Bank–borrower relationship plays an important role in the financial markets (Saparito, Chen, & Sapienza, 2004) (Uzzi & Lancaster, 2003) because they affect decision making and influence the price and availability of credit (Uzzi, 1999). Sociologists examine bank-borrower relationships through focusing on the pattern of social ties within which economic transactions are embedded (Uzzi, 1999)

(Nahapiet & Ghoshal, 1998) (Varun Grover, 2001) have proposed that knowledge transfer is primarily a social phenomenon. By employing this perspective, banks and finance applicants are viewed as being embedded in enduring social relationships that affect their behavior (Gnyawali & Madhavan, 2001; Granovetter, 1985).

The concept of trust is well acknowledged as an integral element in the social capital literature (Coleman James, 1990). In order to achieve their goals, banks need to invest in social capital under the form of trust and trustworthiness. Alternatively trust is one of social capital's outcomes and consequences (Woolcock, 2001). Literature on social capital has different focal interests such as individuals (Inglehart & Baker, 2000) nations (Putnam, 2001) ,cultures (Fukuyama, 1995), and organizations (Fu, 2004)

(Fukuyama, 1997) defined social capital as the a particular set of informal norms or values existed and shared among members of a group that facilitates cooperation among them. Thus Fukuyama does not view social capital as a subset of human capital because it is a property of groups and not individuals. The group endowed with social capital, he argues, may be as small as two friends who share information or collaborate on a common project, and it can be as large as an entire nation. He also argues that the norms that produce social capital must substantively include virtues like truth-telling, the meeting of obligations, and reciprocity.

(Fukuyama, 1997) also has analyzed the relationship between trust, social capital and economic success. He argued that there is cost associated with carrying out an economic exchange due to mistakes, dishonesty, or opportunism. For example, in the context of this study, the more the banks have to pay lawyers to write out detailed financing contracts and the more they have to search for and monitor the behavior of their potential finance seeker, the more costly it becomes to conduct the financing transactions. Fukuyama asserts that the level of trust inherent in national culture can lower transaction cost, which leads to more prosperous economy by promoting market efficiency. (Fukuyama, 1996) has also shown that there exists a positive correlation between the generic level of trust within a society and the economic prosperity of the society.

(Coleman, 1988) defined the concept of social capital as a mixture of several entities that all of which represents some aspect of social structure, and permits certain actions of individual or corporate actors within this structure. He argued that the future obligations and expectations are based on social capital that includes a mutual system of trust as an important component. He also argued that the social structure could help in creating a trustworthy social environment, in opening channels for information, and in setting norms and impose sanctions on social behaviors. He explained the difference between social capital and human capital as the first is relational and embedded in social structure and has public good features. He argued further that social structure turns into social capital when actors effectively invest in it for sake of their interests.

(Putnam, Leonardi, & Nanetti, 1994) defined social capital as several social characteristics of organizations such as trust, norms and networks that can effectively inhance and lubricate the coordinated actions in the society. He further viewed trust as a source of social capital that sustains economic dynamism. In more recent study,

(Putnam, 2001) considered trust as an essential component of norms that arise from social networks. Therefore, he argues that social capital has two primary components namely networks and norms, rather than three components: networks, norms, and trust.

(Hausman, Johnston, & Young, 2006) defines social norms as customary rules of behavior that coordinate interactions between people. He goes on to note that such norms have economic value and become a type of social capital if they create a "uniquely salient or focal solution to a coordination problem, thus reducing the risk of coordination failure. (Woolcock, 2001) identified social capital consist of information, trust, norms of reciprocity inherent in the social networks. (Nahapiet & Ghoshal, 1998) treat trust as a key facet in the relational dimension of social capital.

Apparently, although the above mentioned perceptions of the relationship between social capital and trust, are somehow different, they, however, are conceptually related. This might reveal that there is a close relationship between the both concepts.

8. Definition of Trust

Currently, there is no unified definition of trust that could be used for research. Nevertheless, substantial agreement between scholars exists about some elements that any definition should either include or imply. For example, scholars agree that trust refers to an attitude involving a willingness to expose one's interest to the discretion of others. This willingness is based on a belief, for which there is a degree of uncertainty that potential trustees will avoid using their discretion to harm the interests of the first (Baier, 1986; Coleman James, 1990; Gambetta, 1988; Hardin, 1992)

After reviewing different definitions of trust made in regard to different disciplines the researcher might propose that behavioral trust from Islamic perspective is defined as: : the acceptance of the exposure to the potential occurrence of undesired outcomes of engaging in agreements with others based on tranquil reliance and optimistic expectations that the desired outcomes will be achieved, after exerting the due diligence in gathering and utilizing the available information to mitigate the inherent uncertainty concerning their trustworthiness and ability to fulfill their obligations.

This definition is from the perspective of the trustor, and it views behavioral trust as a decision that trustor needs to make under uncertainty.

The behavioral aspect of trust is manifested by the act of accepting the exposure to the possible occurrence of undesired consequences. This implies that the trustor is aware of that the potential possibility of such occurrence might (or might not) become actual.

The cognitive aspect of behavioral trust is represented by the mitigation of uncertainty that is inherent characteristic in any trust-based agreement. Therefore, as long as the trustor cannot, in anyway, eliminate this inherent uncertainty, he is required to exert the due efforts and diligence in order to alleviate it as much as possible before the engagement in the trust-based agreement. This indicates that the acceptance in this definition concerns the residual uncertainty that is inherent i.e. cannot be eliminated anymore.

The affective or the dogmatic aspect of behavioral trust is represented by the trustor's acceptance to be exposed to unseen factors even though in the case of absence of complete information. In other words, although the trustor cannot be entirely certain, he possesses tranquil reliance and optimistic expectations that, by agreeing to allow the discretion of others, they will demonstrate the due trustworthiness, and employ the required ability in fulfilling their obligations.

The proposed conception of behavioral trust is argued to be modifiable to be suitable to address any context or situation which bears an inherent level of uncertainty. The concern of this article is to address the functional role of behavioral trust in the context of mudarabah financing agreement.

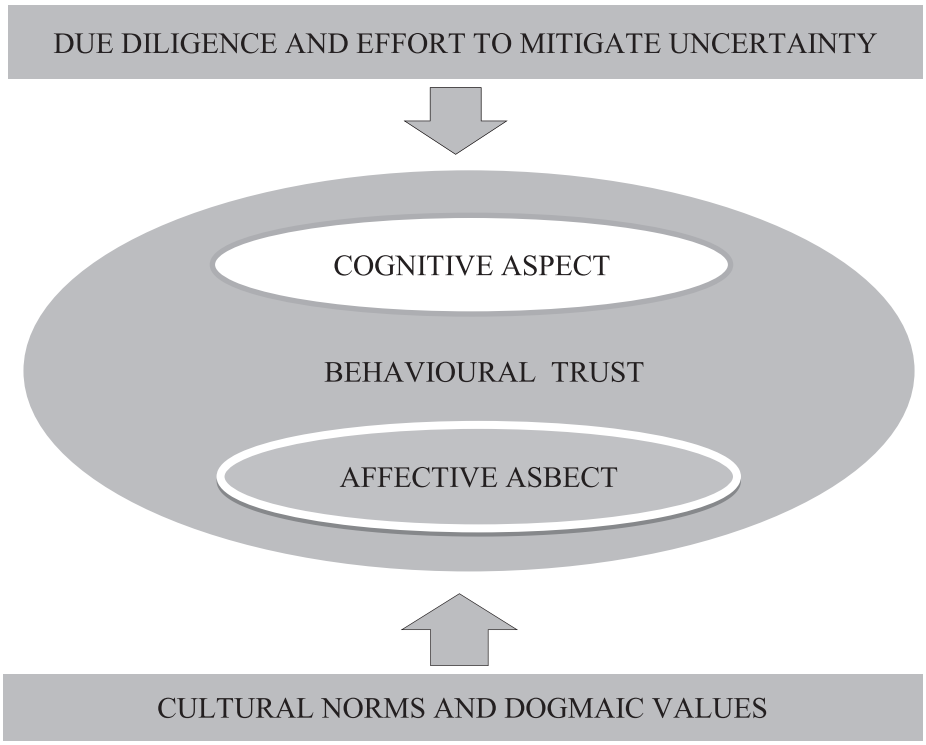
The researcher's proposed modification to suit such context as: The banks' acceptance to be exposed to potential occurrence of adverse selection and moral hazard that are inherent in mudarabah financing agreement, based on tranquil reliance and optimistic expectations that the desired outcomes of this agreement will be achieved, after exerting the due diligence in gathering and utilizing the available information to mitigate the inherent uncertainty concerning the mudaribs' trustworthiness and ability to fulfill their obligations.

In mudarabah financing context, the undesired outcomes are represented by the banks' being potentially exposed to adverse selection and moral hazard due to the asymmetric information regarding the unseen mudarib's traits. The possible due diligence is represented by any possible deliberate efforts that could be exerted in utilizing the available information, such as monitoring rather than controlling the mudarib's acts, carefully assessing the mudarib's entrepreneurial

skills and other personal traits. The desired outcomes represent any outcome the bank management considers to achieve by implementing the mudarahah financing mode such as increasing the credit availability, promoting certain economic sectors, assuming the social responsibility, or complying with the spirit of shariah and attending to shariah objectives.

Finally, the Islamic-based view proposed above introduces behavioural trust as it is driven by an aim of investing in the social capital under the form of trustworthiness. The investment in social capital is in order to achieve mutual benefits for all parties, where the complete information about the future contingencies are impossible be obtained. Thus this conception is different of the conventional one which viewing trust as a matter of gambling or assuming risk. In other words, the bank as capital provider does not or, more specifically, is not able to obtain complete certainty regarding the trustworthiness and intention of the mudaribs (being an unseen matter) but, instead, he only assumes positively the trustworthiness quality to be available as a common quality of mudaribs, rather than expecting or conceiving them as betrayers or evils, and this is merely because the capital provider positively think that the mudarib will not deny the rights or breach the covenants. Additionally, the above proposed conception asserts the concept of reliance, as a faith-based or dogmatic element, to be the indispensable and the sole component without which the decision to assume the potential unfavourable contingencies i.e. the decision to behaviourally trust cannot be made. Thus, reliance as a faith-based or dogmatic element is alone what compensates the bounded rationality of the capital provider and renders the behavioural trust a meaningful concept. Figure 2.1 represents the proposed research. A conceptual framework might be proposed as in the Figure 1.

Figure 1: Conceptual framework of functional role of the trust



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